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In the Supreme Court of the United States

OCTOBER TERM, 1950

No. 437

E. T. RENFRO DRUG COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Court of Appeals (R. 136-143) is reported at 183 F. 2d 846. The findings of fact and opinion of the Tax Court of the United States (R. 29-37) are reported at 11 T.C. 994.

JURISDICTION

The judgment of the Court of Appeals was entered on July 27, 1950 (R. 143). A petition for rehearing (R. 144-161) was denied on September 13,

1950 (R. 162). The petition for a writ of certiorari was filed on December 6, 1950. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether, in the computation of the excess profits tax credit on the income method, taxpayer is entitled to the base period experience of four predecessor partnerships, the answer to which under Code Section 742 depends on whether under Section 740 taxpayer was an "acquiring corporation" of which each partnership was a "component corporation."

STATUTE AND REGULATIONS INVOLVED

These are set out in the Appendix, *infra* pp. 11 to 18.

STATEMENT

The material facts as found by the Tax Court (R. 30-34) are as follows:

The taxpayer is a corporation incorporated under the laws of Texas with its principal office in Fort Worth, Texas. Its books are kept, and its federal income and excess profits tax returns are filed, upon an accrual basis, and upon the basis of the calendar year. (R. 30.)

The taxpayer was originally incorporated in or about the year 1919 as "Renfro Drug Store No. 5," with authorized and issued capital stock of $28,000. It has since engaged in the drug business at Fort

Worth, Texas. In 1939, the taxpayer increased its authorized capital stock from $28,000 to $433,000 and through the issuance of such increased capital stock, it acquired the assets and business of some twenty-one partnerships and two corporations, all of which were engaged in the drug business. Among these partnerships so acquired was a group of four referred to as the "Wren Group," also known as Stores Nos. 1, 9, 15 and 20. (R. 30.)[1] On January 1, 1939, Inez Renfro, Inez Renfro Allen and C. L. Wren were equal partners, each owning a one third interest in these four partnerships. (R. 31.)

In October 1939, Inez Renfro and Inez Allen entered into a verbal agreement to purchase the interest of Wren in the partnerships. It was agreed that this sale should be effective as of December 31, 1939, and that Wren should receive the book value of his interest in the partnerships as of the close of business on that day, according to a formula agreed upon by the parties. To apply this formula time was necessary after the close of business on the effective date, so that a bill of sale was not actually delivered by Wren to Inez Renfro and Inez Allen until February 3, 1940. (R. 31-32.)

On February 14, 1940, Inez Renfro and Inez Allen conveyed to the taxpayer solely in exchange for 574.33 shares of the common stock of the tax-

[1] Only the four partnerships of the so-called Wren Group were in dispute in the Court of Appeals or are involved in this proceeding.

payer corporation, to be issued one half to Inez Renfro and one half to Inez Allen, all of their interest in and to the business properties and the partnerships of the Wren stores. The bill of sale to the taxpayer from Inez Allen and Inez Renfro was effective as of the close of business December 31, 1939. (R. 32.)

The $19,144.65 paid to Wren for his interest in the Wren partnerships was advanced by the taxpayer corporation on behalf of Inez Renfro and Inez Allen but these advancements were subsequently repaid to the taxpayer and the actual cash outlay to Wren was borne by Inez Renfro and Inez Allen personally. (R. 32.)

After the transfer to the taxpayer of the Wren stores, Inez Renfro and Inez Allen owned in equal amounts more than 80 per cent of the authorized issued and outstanding capital stock of the taxpayer corporation. (R. 33.)

In his determination (R. 10-22) of the taxpayer's income and excess profits tax liabilities for the years 1942 and 1943,[2] the Commissioner eliminated (R. 13, 15) from the computation of the taxpayer's average base period net income the base period net incomes of the four partnerships

---

[2] These are the two taxable years involved, but the actual computation goes into the years 1940 and 1941 (R. 20-22) in order to arrive at the amount of the taxpayer's *unused* excess profits credit which is allowed as a credit in 1942 in computing the excess profits tax due for that year (R. 16).

operating Stores Nos. 1, 9, 15 and 20, and determined the resulting deficiencies.[3]

The Tax Court held in a decision reviewed by the full court, one judge dissenting (R. 37), that the taxpayer was not entitled to use the base period experience of the partnerships in computing its excess profits credit for the taxable years. The Court of Appeals, one judge dissenting, affirmed. (R. 138.)

ARGUMENT

Section 742 of the Internal Revenue Code (Appendix, *infra,* p. 14), permits an "acquiring corporation" to use the base period income experience of its "component" corporations for the purpose of computing the excess profits tax credit on the income method under Section 713. Both courts below held that the assets of the four Wren partnerships passed through a partnership or a joint proprietorship, consisting of Inez Renfro and Inez Allen, which could not under the definition of acquiring corporation in Section 740(a)(1)(D) and (g) (Appendix, *infra,* pp. 12-13), pass on to taxpayer the base period income experience of the four Wren partnerships, which it seeks to utilize. This result is plainly correct on both the statutory

---

[3] In arriving at the amount of the credit, the Commissioner made a further adjustment, giving the taxpayer the benefit of the so-called "75% rule" under Section 713 (e) of the Code, in increasing the taxpayer's lowest base period year (1939) to an amount equal to 75% of the average for the other three years. (R. 15.)

language and its purpose; it is expressly directed by a contemporaneous Treasury Regulation; and there is no conflict.

1. The statute requires this result because, although a partnership can be a component corporation (Section 740(b)(5) Appendix, *infra,* p. 13), there is no definition of acquiring corporation (Section 740(a)) which includes a partnership. Thus, under the scheme of Supplement A,[4] there is no method for transmitting the base period experience of a component of a component partnership (Section 740(g), Appendix, *infra,* p. 13). The chain is broken because the new partnerships or joint proprietorships could not be acquiring corporations. This result is expressly provided by Section 35.740-4 of Treasury Regulations 112 (Appendix, *infra,* pp. 16-18), which, under familiar principles, is entitled to great weight as a contemporaneous interpretation of a statute by those charged with its administration.

Moreover, this case is not within the Congressional purpose (as evidenced by the statutory structure, the Committee Reports, and the Regulations) in permitting a taxpayer to use the base period income experience of another. The purpose was to grant this unusual privilege where the taxpayer operated not only the same business, but was controlled by the same interests as the prede-

[4] Sections 740 and 742 of the Internal Revenue Code constitute Supplement A.

cessor. See Treasury Regulations 112, Sec. 35.740-2(b) (Appendix, *infra,* p. 18); H. Rep. No. 146, 77th Cong., 1st Sess., pp. 4, 14 (1941-1 Cum. Bull. 550); S. Rep. No. 75, 77th Cong., 1st Sess., pp. 4, 14-15 (1941-1 Cum. Bull. 564). Thus the continuity of interest requirement of Section 112(b)(5) (Appendix, *infra,* p. 11), made a condition on the applicability of Section 740(a)(1)(D), was plainly violated when Mrs. Renfro and Mrs. Allen purchased Wren's interests, even if it be assumed with taxpayer that no new partnership resulted by the change in the identity of the partners.[5]

2. There is no "conflict" with the principles

[5] If it be assumed, as the dissenting judge did below (R. 142), that the substance of the transaction was that all three partners transferred the partnership assets to the taxpayer, each receiving his pro rata share of the stock, and that Wren then transferred his stock to his two partners, in this situation also the taxpayer could not be held to be an "acquiring corporation". On well-settled principles, the proportionate interest and control requirements of Section 112(b)(5) would have been violated, since as a part of the same plan the stock of one of the transferors would have been immediately transferred to others. Cf. *Bassick* v. *Commissioner,* 85 F. 2d 8 (C. A. 2), certiorari denied, 299 U. S. 592; *West Texas Refining & D. Co.* v. *Commissioner,* 68 F. 2d 77 (C. A. 10); *Hazeltine Corp.* v. *Commissioner,* 89 F. 2d 513 (C. A. 3). On this assumption, the proportionate interest requirements under the cited cases would not be met because those owning two-thirds of the assets transferred received all of the stock, a situation plainly not within Section 112(b)(5). See *Mather & Co.* v. *Commissioner,* 171 F. 2d 864 (C. A. 3), certiorari denied, 337 U. S. 907; *Bodell* v. *Commissioner,* 154 F. 2d 407 (C. A. 1); *United Carbon Co.* v. *Commissioner,* 90 F. 2d 43 (C. A. 4); *Snead* v. *Jackson Securities & Investment Co.,* 77 F. 2d 19 (C. A. 5), certiorari denied, 296 U. S. 599. The control requirements would not be met, because the statute contemplates that the transferors as a group must be in control.

announced in *Ransohoffs, Inc.* v. *Commissioner,* 9 T.C. 376, because, as the Tax Court itself noted in the decision below (R. 36), the partnership agreement in that case specifically provided that the partnership should continue after the death or withdrawal of the partner. Accordingly, the problem of this case, whether the base period experience of a partnership can be transmitted to a taxpayer through another partnership consisting of different members, was not involved.

3. There is no merit either in the contention (Pet. 7-9) that the court below failed to apply the principles announced in *Heiner* v. *Mellon,* 304 U.S. 271, and applied in *Rossmoore* v. *Anderson,* 67 F. 2d 1009 (C.A. 2d), affirming 1 F. Supp. 35 (S.D. N.Y.). Taxpayer's contention that the old partnerships continued in a liquidating status after the withdrawal of Wren fails on the facts found by the Tax Court and approved by the Court of Appeals. In any event, the problem in this case is utterly foreign to that of *Heiner* v. *Mellon, supra,* where the question was simply whether income could be realized before the partnership had completed the liquidation of a corporate business where the partnership was expressly organized to accomplish the liquidation.

4. Nor is there merit in taxpayer's broad contention (Pet. 9-11) that the decision below conflicts with the "entity theory" of partnership which should be applied for all tax purposes.

Even if the contention were generally accurate, taxpayer misconceives the nature of the theory because, as it would apply the concept here, it assumes that a partnership continues as the same business entity regardless of the number or nature of substitutions or withdrawal of partners and regardless of state law provisions, just as a corporation continues to exist notwithstanding changes in ownership. The theory is patently untenable and it is directly inconsistent with *Guaranty Trust Co.* v. *Commissioner,* 303 U.S. 493. The cases which taxpayer cites as establishing an "entity theory" of partnership (Pet. 9-10) in general deal with the entirely different problem of the nature of a partner's gain or loss on the sale of his partnership interest and, in any event, even within this precise field, this Court, as recently as January 2, 1951, denied petitions for certiorari based on an alleged conflict in decisions. *Commissioner* v. *Swiren,*[6] No. 416, October Term, 1950; *First Nat. Bank of Mobile* v. *Commissioner,*[7] No. 342, October Term, 1950.

5. Finally, there is no merit in the contention (Pet. 12) that the decision below violates the principle of *Burnet* v. *Harmel,* 287 U.S. 103, that in the absence of language evidencing a different purpose, the revenue laws are to be interpreted without resort to state law. It does not appear that the court below placed the decision on state law,

[6] 183 F. 2d 656 (C. A. 7th).
[7] 183 F. 2d 172 (C. A. 5th).

but in any event it is plain that no different result would obtain here whether tested by the law of Texas (that a partnership dissolves on withdrawal of a member) or by a uniform interpretation of "partnership" in Supplement A based on the statutory purpose.

CONCLUSION

The decision below is correct and there is no conflict of decisions. The petition should be denied.

Respectfully submitted,

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JANUARY, 1951.

APPENDIX

Internal Revenue Code:

CHAPTER 1—INCOME TAX

* * * * *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

* * * * *

(b) *Exchanges Solely in Kind.*—

* * * * *

(5) [as amended by Section 213 (c) of the Revenue Act of 1939, c. 247, 53 Stat. 862] *Transfer to corporation controlled by transferor.*—No gain or loss shall be recognized if property is transferred to a corporation by one or more persons solely in exchange for stock or securities in such corporation, and immediately after the exchange such person or persons are in control of the corporation; but in the case of an exchange by two or more persons this paragraph shall apply only if the amount of the stock and securities received by each is substantially in proportion to his interest in the property prior to the exchange. * * *

* * * * *

(h) *Definition of Control.*—As used in this section the term "control" means the ownership of stock possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and at least

80 per centum of the total number of shares of all other classes of stock of the corporation.

* * * * *

(26 U. S. C. 1946 ed., Sec. 112.)

CHAPTER 2—ADDITIONAL INCOME TAXES

* * * * *

SUBCHAPTER E—EXCESS PROFITS TAX

[As added by Section 201 of the Second Revenue Act of 1940, c. 757, 54 Stat. 974, which provided that the new subchapter may be cited as the "Excess Profits Tax Act of 1940"]

PART I

* * * * *

PART II—RULES IN CONNECTION WITH CERTAIN EXCHANGES

SUPPLEMENT A—EXCESS PROFITS CREDIT BASED ON INCOME

SEC. 740 [as amended by Section 228 (a) of the Revenue Act of 1942, c. 619, 56 Stat. 798].

DEFINITIONS.

For the purposes of this Supplement—

(a) *Acquiring Corporation.*—The term "acquiring corporation" means—

(1) A corporation which has acquired—

* * * * *

(D) substantially all the properties of a partnership in an exchange to which section 112 (b) (5), or so much of section 112 (c) or (e) as refers to section 112 (b) (5), or to which a corresponding provision of a prior revenue law, is or was applicable.

* * * * *

(b) *Component Corporation.*—The term "component corporation" means—

* * * * *

(5) In the case of a transaction specified in subsection (a) (1) (D), the partnership whose properties were acquired.

* * * * *

(g) *Component Corporations of Component Corporations.*—If a corporation is a component corporation of an acquiring corporation, under subsection (b) or under this subsection, it shall (except for the purposes of section 742 (d) (1) and (2) and section 743 (a) (1), (2), and (3)) also be a component corporation of the corporation of which such acquiring corporation is a component corporation.[8]

(h) *Sole Proprietorship.*—For the purposes of sections 740 (a) (1) (D), 740 (b) (5), and 742 (g), a business owned by a sole proprietorship shall be considered a partnership.

(26 U. S. C. 1946 ed., Sec. 740.)

---

[8] The provisions referred to in the parenthetical clause in Sec. 740 (g) are not relevant to the question in this case.

SEC. 742 [as amended by Section 228 (c) of the Revenue Act of 1942.] SUPPLEMENT A AVERAGE BASE PERIOD NET INCOME.

In the case of a taxpayer which is an acquiring corporation, its average base period net income (for the purpose of the credit computed under section 713) shall be the amount computed under section 713 or the amount of its Supplement A average base period net income, whichever is the greater. The Supplement A average base period net income shall be the amount computed without regard to subsection (h) of this section or computed under subsection (h) of this section, whichever is the greater. The Supplement A average base period net income shall be computed as follows:

* * * * *

(g) In the case of a partnership which is a component corporation by virtue of section 740 (b) (5), the computations required by this Supplement shall be made, under rules and regulations prescribed by the Commissioner with the approval of the Secretary, as if such partnership had been a corporation. For the purpose of such computations, in making the adjustment for income taxes required by section 711 (b) (1) (A), the partnership so regarded as a corporation shall be considered as having distributed all its net income as a dividend.

* * * * *

(26 U. S. C. 1946 ed., Sec. 742.)

Treasury Regulations 111 (relating to the Income Tax), promulgated under the Internal Revenue Code:

SEC. 29.112 (b) (5)-1. *Transfer of Property to Corporation Controlled by Transferor.*—As used in section 112 (b) (5), the phrase "one or more persons" includes individuals, trusts or estates, partnerships and corporations (see section 3797); and to be in "control" of the transferee corporation such person or persons must own immediately after the transfer stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of shares of all other classes of stock of such corporation. (See section 112 (h).) The phrase "immediately after the exchange" does not necessarily require simultaneous exchanges by two or more persons, but comprehends a situation where the rights of the parties have been previously defined and the execution of the agreement proceeds with an expedition consistent with orderly procedure.

* * * * *

SEC. 29.112 (h)-1. *Control of Corporation.*—Section 112 (h) defines the term "control" in reference to the phrase "control of the corporation," as used in section 112 (b) (5) and section 112 (g) (1). It is provided specifically that this definition is limited to the meaning of the term "control" as that term is used in section 112.

Treasury Regulations 112 (relating to the Excess Profits Tax), promulgated under the Internal Revenue Code:

> SEC. 35.740-1 *Purpose and Scope of Supplement* A.—(*a*) The term "Supplement A", when used in these regulations, means sections 740 and 742 to 744. Supplement A provides rules governing the right to use the excess profits credit based on income and the method of computing such credit, in the case of certain "acquiring" corporations. An acquiring corporation is a domestic corporation which has absorbed one or more other domestic corporations, partnerships, or businesses owned by sole proprietorships in a transaction meeting the requirements set forth in section 740 (a), which transaction is generally referred to in these regulations as a "Supplement A transaction." Each such absorbed corporation, partnership, or business owned by a sole proprietorship is designated a component corporation of the acquiring corporation. Furthermore, except for the purposes of section 742 (d) (1) and (2) and section 743 (a) (1), (2), and (3), if an acquiring corporation is later absorbed by another acquiring corporation, all of the component corporations of the first acquiring corporation become component corporations of the second acquiring corporation. * * *
>
> (*b*) The purpose of Supplement A is in general to attribute to an acquiring corporation the existence of corporations, partnerships, or businesses owned by sole proprietorships absorbed by it, together with the base

period excess profits net income or deficit in excess profits net income and the net capital changes of such predecessors, in order (1) that a corporation the corporate life of which in substance, though not in form, includes the base period may use the excess profits credit based on income and (2) that a corporation composed in whole or in part of component corporations may compute its excess profits credit in the light of the base period experience of the entire enterprise. * * *

SEC. 35.740-2 *Transactions Whereby a Corporation Becomes an Acquiring Corporation.* —(*a*) The types of transactions whereby a corporation can become an acquiring corporation are specifically described in section 740 (a). In addition to statutory mergers and consolidations and the acquisition of property in a complete liquidation in which gain or loss is not recognized because of the provisions of section 112 (b) (6) or the same section as contained in the Revenue Act of 1936 or 1938, only the following types of transactions are included.

* * * * *

(4) The acquisition of substantially all the properties of a partnership in an exchange to which section 112 (b) (5), or so much of section 112 (c) or (e) as refers to section 112 (b) (5), or to which the corresponding provisions of a prior revenue law, is or was applicable. For the purposes of this paragraph a business owned by a sole proprietorship shall be considered a partnership.

(*b*) The types of transactions set forth in section 740 (a), other than those set forth in section 740 (a) (1) (C), either are embraced within the definition of a reorganization contained in section 112 (g) (1), are transfers to a controlled corporation within the meaning of section 112 (b) (5) and related sections, or are complete liquidations within the meaning of section 112 (b) (6). Since Supplement A applies only to cases where there is a sufficient continuity of interest to justify treating a corporation by which the assets of another corporation, a partnership, or a business owned by a sole proprietorship have been acquired, as standing in the place of its predecessor, such transactions must satisfy all the requirements of the regulations prescribed under section 112 with respect to such transactions in order that the transferee corporation may be treated as an acquiring corporation.

SEC. 35.740-4 *Partnerships and Sole Proprietorships Under Supplement A.*—A partnership (or a business owned by a sole proprietorship) can be a component corporation for the purposes of Supplement A, subject to the exceptions in section 740 (g). However, a partnership (or a business owned by a sole proprietorship) cannot be an acquiring corporation and, therefore, section 740 (g) cannot operate to make any of its predecessors component corporations of its acquiring corporation.

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Reply Argument

(1) The statute did not require the holdings below 2

(2) The opinion of the Tax Court below conflicted with its decision in Ransohoff's, Inc. v. Commissioner of Internal Revenue, 9 T.C. 376 4

(3) The opinion and decision below failed to apply the principles announced in Heiner v. Mellon, 304 U.S. 271, and Rossmoore v. Anderson, 67 F. 2d 1009 7

(4) There is no merit in respondent's assertion that petitioner's contentions are inconsistent with Guaranty Trust Company v. Commissioner of Internal Revenue, 303 U.S. 493 8

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No. 437

IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1950

E. T. RENFRO DRUG COMPANY,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

PETITIONER'S REPLY TO BRIEF FOR THE RESPONDENT IN OPPOSITION

Preliminary Statement

Under date of January ——, 1951, respondent filed in this Court his brief in opposition to the petition of E. T. Renfro Drug Company for a writ of certiorari

to the United States Court of Appeals for the Fifth Circuit. Respondent's brief contains matter we feel should be answered. Accordingly, as concisely as is possible, we will hereinafter deal seriatim with the points made in respondent's brief.

Reply Argument

(1) Respondent asserts: (a) That the statute required the Court below to deny to taxpayer the base period earning experience of the four Wren partnerships because, under the scheme of Supplement A of the Internal Revenue Code, there is no method for transmitting the base period experience of a component partnership; and (b) that this case therefore is not within the Congressional purpose in permitting a taxpayer to use the base period experience of another.

In so contending, respondent adopts the type of logic and method of argument condemned by Judge Hutcheson in his dissenting opinion below, namely, argument by label. He assigns the label, "component of a partnership," to the four Wren partnerships and proceeds from this untenable premise[1] to a foregone (and adverse) conclusion.

---

[1] While "dissolved" by Wren's withdrawal, the four Wren partnerships were not "terminated" thereby. *Heiner* v. *Mellon*, 304 U.S. 271; *Rossmore* v. *Anderson*, 67 F. 2d 1009 (C. A. 2d), affirming 1 Fed. Supp. 35 (S.D. N.Y.). They continued in existence until their assets and businesses were transferred to E. T. Renfro Drug Company. Before this transfer occurred, Mrs. Renfro and Mrs. Allen had acquired by assignment from Wren his partnership interest, which included the right to receive his share of the surplus of the

The intent and purpose of the Congress in enacting Supplement A (Sections 740 and 742) of the Internal Revenue Code is concisely and fairly set out in the Treasury's own regulations, referred to at page 6 of respondent's brief and printed verbatim at pages 16 and 17 of his brief.

The applicable language of the mentioned regulation, to-wit: Section 35.740-1(b) of Treasury Regulations 112, is:

> "The purpose of Supplement A is in general to attribute to an acquiring corporation the existence of * * * partnerships * * * absorbed by it, together with the base period excess profits net income or deficit in excess profits net income and the net capital changes of such predecessors in order * * * that a corporation composed in whole or in part of component corporations (including absorbed partnerships) may compute its excess profits credit in the light of the base period experience of the entire enterprise. * * * " (Matter in parentheses supplied.)

Sections 740 and 742 of the Internal Revenue Code, applied in the spirit in which they were enacted by

four Wren partnerships upon their termination. There were no intervening partnerships or joint proprietorships. *Commissioner of Internal Revenue* v. *Lehman*, 165 F. 2d 383, pp. 386, 387. The transfer of the four partnerships by Mrs. Renfro and Mrs. Allen to petitioner corporation came squarely within the provisions of Section 112(b) (5), Internal Revenue Code.

the Congress, accord to petitioner the benefit of the base period experience of the four Wren drug stores, operated as separate partnerships during the base period and in corporate form by petitioner (as a component of its entire enterprise) during the years in which the wartime excess profits taxing Acts were in effect. The decision below, which held to the contrary, should be reversed.

(2) Respondent contends (Brief, pages 7 and 8) that there is no conflict in the opinion of the Tax Court below with the principles announced in *Ransohoff's, Inc.* v. *Commissioner*, 9 T.C. 376, because, "as the Tax Court itself noted in the decision below (Record, page 36), the partnership agreement in that case specifically provided that the partnership should continue after the death or withdrawal of the partner."

In essence, this line of argument is tantamount to asserting that: (a) The original Wren partnerships did not remain in existence for any period whatever, or for any purpose, after Wren's withdrawal; or else, (b) that their continued existence, to be effective for the purposes of Supplement A of the Internal Revenue Code, must have been by express agreement of the parties and that it was not sufficient for their continued existence to have resulted from settled general principles of law.

As its foundation, the first of the foregoing propositions necessarily assumes—and this is equally true of the decisions of the Tax Court and the Court of Appeals below—that upon the withdrawal of Wren from the four Wren partnerships, the partnerships vanished into thin air, leaving no assets to be disposed of, liabilities to be discharged, or business to be wound up. Obviously, this was not the case. The four partnerships continued to exist (*Heiner* v. *Mellon*, *supra*; *Rossmoore* v. *Anderson*, *supra*) until they were wound up through the conveyance of their assets to petitioner corporation by a transfer of the type described in Section 112(b)(5) of the Internal Revenue Code.

The second proposition—if it be actually relied upon by the respondent—has no support in any statute, regulation or judicial decision.

Admittedly, the decision of the Tax Court in *Ransohoff's, Inc.* and its decision in the case below were diametrically opposite. With one exception, however, the underlying material facts were substantially identical, as is shown by the following comparison:

Ransohoff's, Inc.	*Wren Partnerships*
1. Written partnership agreement.	Partnership agreement oral.
2. Originally three partners.	Originally three partners.
3. One partner died.	One partner withdrew.
4. Surviving partners with outside funds acquired deceased partner's interest in partnership surplus, by paying to executor of decedent's estate the book value of decedent's partnership interest.	The remaining partners, with outside funds, acquired the interest of the withdrawing partner by paying to him the book value of his partnership interest.
5. After interval of approximately two years, assets and business of partnership transferred to corporation for its stock, issued equally to surviving partners.	After a short interval, assets and businesses of four partnerships transferred to petitioner corporation for its stock, issued equally to remaining partners.
6. After transfer, transferring partners in control of transferee corporation.	After transfer, transferring partners in control of transferee corporation.

From the foregoing comparison, it will be seen that the only difference in the material facts in the two cases was that in one case the written agreement provided that the death or withdrawal of the partner did not dissolve or terminate the partnership, while in the other case, the oral partnership agreements were silent on this point. Did this single difference justify the divergent decisions of the Tax Court in the two cases?

Realistically appraised, the sole office and effect of a provision in a partnership agreement, or in a statute, that the death or withdrawal of a partner will not dissolve or terminate the partnership, is to divest the withdrawing partner or the estate of a deceased partner of the right, forthwith, to require the cessation of all new business; and further, to divest them of the right to require the immediate liquidation of the partnership assets. With or without such a provision in the partnership agreement or controlling statute, once a partnership is validly organized and constituted, it continues to exist until it is not only *dissolved*, but its assets are marshalled and the partnership *terminated* by the distribution of its surplus to those entitled to receive it. In the case at bar, as in the *Ransohoff's, Inc.* case,[2] this was done by transferring the assets and businesses of the four Wren partnerships to petitioner corporation in a transaction of the type described in Section 112(b)(5), Internal Revenue Code.

Clearly, in principle the decision of the Tax Court below was directly contrary to its decision in *Ransohoff's, Inc.* v. *Commissioner, supra.*

(3) Respondent (Brief, page 8) asserts that the contention of petitioner that the Court below failed to apply the principles announced in *Heiner* v. *Mellon*,

[2] The only readily discernable difference attributable to the partnership agreement provision discussed is that, because of it, the time intervening between the death of the Ransohoff partner and the transfer of the partnership assets to a corporation was far greater than the interval between the withdrawal of Wren and the transfer of Wren partnerships assets to petitioner corporation.

supra, and *Rossmoore* v. *Anderson*, *supra*, which in turn was founded on taxpayer's contention that the old partnerships continued in a liquidating status after the withdrawal of Wren, "fails, on the facts found by the Tax Court and approved by the Court of Appeals." We think it sufficient reply to this assertion to point out that what respondent designates a finding af fact was in truth a mere conclusion of law (viz., that the withdrawal of Wren from the four Wren partnerships, without anything more occurring, had the effect of creating new partnerships or joint proprietorships between the remaining partners).

Tested in the light of the principles announced and applied by this Court in *Heiner* v. *Mellon*, *supra*, and by the Court of Appeals for the Second Circuit in *Rossmoore* v. *Anderson*, *supra*, this was an erroneous conclusion of law. As the decision below turned entirely upon such wholly erroneous conclusion of law, and was therefore wrong, it should be reversed by this Court and not left, unreversed, to becloud basic principles of decision in an important field of Federal taxation.

(4) At pages 8 and 9 of his brief, respondent says that the contention of petitioner that the decision below conflicts with the "entity theory" of partnership, which should be applied for all tax purposes, is patently untenable and is directly inconsistent with *Guaranty Trust Company* v. *Commissioner*, 303 U.S. 493.

It is difficult to see how respondent gets any comfort ...t of *Guaranty Trust Company* v. *Commissioner*,

supra,[3] which tends to support, rather than undermine, petitioner's contentions. Moreover, that case is an excellent example of the cause and results of what is sometimes described as a "hard"case. The decision of the Court was by five judges. Two of the judges of the Court (Mr. Justice Cardoza and Mr. Justice Reed) took no part in the consideration or decision of the case. Two judges (Mr. Justice McReynolds and Mr. Justice Roberts) dissented. The question before the Court was whether certain partnership income might be included in, or must be excluded from, the taxable income of a deceased taxpayer. It was not taxable to anyone else. The taxpayer, decedent's executor, asked the Court to apply a rule of statutory construction that would permit serveral months' taxable income to escape tax. This the Court refused to do. It authorized the taxing of the income in question, by construing the term "accounting period" of the partnership in such a fashion as to fit the needs of the occasion, holding that as to a deceased partner the accounting period of the partnership ended with his death (although the accounting period of the partnership as to the surviving partners is not affected thereby; *cf. Mary D. Walsh* v. *Commissioner*, 7 T.C. 205.).

[3] It is worthy of note that in *Guaranty Trust Company* v. *Commissioner*, the Court dealt with a partnership in which one new member had been admitted and one old member had died, as a single (one and the same) partnership. It concerned itself solely with the question: What was the "accounting period" (or periods) of that partnership, and how were the time and manner of reporting partnership income affected thereby? If the death of a partner had terminated, as well as dissolved, the partnership, the question there before the Court would have answered itself.

Guaranty Trust Company v. *Commissioner* (while it served a laudable purpose), by setting up the anomalous situation that a partnership's "accounting period" might, because of extraneous circumstances, differ as between different members of the partnerships, introduced complexities of reasoning that have bedeviled the interpretation and application of the taxing Acts to partners and partnerships ever since its decision. The loophole it sought to close has since been cured by Section 126 of the Internal Revenue Code. Having outlived its purpose, *Guaranty Trust Company* v. *Commissioner* should be overruled, or at least the generality of its language should be severely limited by this Court.

Conclusion

Cases involving the impact of the Federal income tax on partnerships and partners are coming before the courts in ever-increasing numbers. In many instances lurking someplace in each of these cases—indeed, frequently responsible, directly or indirectly, for the existence of the litigation—is a clash between the concepts of the ancient "partner's undivided interest in each specific partnership asset" theory (dear to the heart of the Treasury Department, although consistently repudiated by the courts) and the more modern "entity theory," upon which (*cf.* *Commissioner* v. *Lehman*, 165 F. 2d 383) Congress fitted the taxation of partnerships.

Foreseeable litigation in the field of partnership taxation may be obviated by a forthright decision by

this Court to the effect that for Federal tax purposes a partnership is a tax-computing entity which, once formed, continues to exist until it not only is dissolved, but, also, terminated by the liquidation of its assets. This it can do by reversing the decision below.

For the foregoing reasons, and those set out in the petition therefor, a writ of certiorari to the Court of Appeals for the Fifth Circuit should be granted.

Respectfully submitted,

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